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Deposited in DRO:

22 October 2019

Version of attached file:

Accepted Version

Peer-review status of attached file:

Peer-reviewed

Citation for published item:

Lai, Karen P.Y. and Pan, Fenghua (2021) 'Brexit and shifting geographies of financial centres in Asia.', *Geoforum.*, 125 . pp. 201-202.

Further information on publisher's website:

<https://doi.org/10.1016/j.geoforum.2018.02.004>

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Brexit and shifting geographies of financial centres in Asia

Published as Lai, Karen P.Y. and Pan, Fenghua (2018) '[Brexit and shifting geographies of financial centres in Asia](https://doi.org/10.1016/j.geoforum.2018.02.004)', *Geoforum*, <https://doi.org/10.1016/j.geoforum.2018.02.004>

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Abstract: Brexit might have profound impacts on the global financial landscape, as the global economy and financial markets are increasingly inter-connected. London's role as the top international financial centre in Europe, could be threatened due to the uncertain consequences of Brexit. Therefore, the geographies of Asian financial centres might be shifted as a result of Brexit, because London plays a central role in the existing global financial centre networks and many Asian financial centres, such as Hong Kong and Singapore, have strong financial connections with London. On the one hand, how Asian financial centres are linked with London and other European financial centres is key to understanding the potential impacts of Brexit on them. On the other hand, the reactions to Brexit of Asian economies, in particular, China, will also influence the role of London as a financial centre. It will in turn influence the geographies of financial centre in Asia.

Keywords: Brexit, Financial Centre, Financial Geography, Asia

The impact of Brexit on financial centres in Asia will depend on changes in business orientation of British and European banks, as well as non-financial firms, following Brexit negotiations and regulatory changes (as discussed by Hall and Wójcik, and Dörny and Dymksi in this issue). The activities of banking and finance have facilitated much of the global spread

of trade, production and consumption activities over the past few decades, and financial institutions themselves have also become highly globalised in their firm structures and business operations. However, domestic markets and economies are still vital for many so-called ‘global’ banks; despite the attraction of a growing Asian market for financial products and services, the importance of home country effect on firm operations cannot be underestimated. We have already witnessed this trend from major US and European banks, e.g. Morgan Stanley, UBS, Deutsche Bank, Barclays, which made major cutbacks on international operations following the 2008 global financial crisis and Eurozone crisis. After 20 years of massive growth and financial globalisation, many of the big global banks have become arguably less ‘global’ as they refocus on core business segments particularly in home markets, dispose of non-core assets, raise capital ratios, and find ways to tap into new and profitable markets without overcommitting to expensive office networks and large teams. Such consolidation of banking networks and operations will likely negatively affect smaller financial centres in Asia, e.g. Bangkok, Kuala Lumpur, Taipei, Mumbai, while favouring larger financial centres. Singapore and Hong Kong, which already play important roles as regional headquarters coordinating market analysis, financial transactions and client networks across Asia, could instead see increased firm responsibilities and business coverage as banks make the most out of those prime locations.

As the largest economy in Asia and second largest economy in the world, economic activities in China and the growing demand for financial services will have significant impact on global financial activities. The last decade has witnessed distinctive overseas expansion of Chinese firms. Recently, the “Belt and Road” initiative has become a key national agenda, which will continue to push Chinese firms to go abroad. The growing participation of Chinese firms in international trade and outward FDI has led many Chinese financial firms to follow their domestic clients globally. In addition, the Chinese government has been pushing for the internationalisation of the Renminbi (RMB). Chinese financial firms, especially large state-owned banks, have played prominent roles in this, which has contributed to the significant growth of Chinese overseas banking activities and the reconfiguration of market making in international financial centres (Hall, 2017). The continuing internationalisation of RMB and global expansion of Chinese financial services firms could reshape the geography of global finance and the future of existing and potential international financial centres outside of China.

China has strong economic ties with the UK and Brexit will complicate these relationships. Amongst European countries, the UK has the largest stock of investments from

China. It also has the largest number of Chinese bank branches, with London holding the top position in 2015. Brexit negotiations to date has already revealed increased competition amongst European cities to attract financial business away from London (see Dörny and Dymski in this issue). Following Brexit, Chinese firms will likely think twice about their locational strategies when they enter European markets. In particular, when firms set up regional headquarters in Europe, London might not enjoy the same locational advantage as before. To avoid the uncertainties of Brexit, Chinese financial and non-financial firms might opt for other financial centres in Europe, which could create greater opportunities for Frankfurt, Luxemburg, Paris and other European cities to obtain more financial functions within Europe. Moreover, the power of agglomeration economies suggest that existing Chinese financial firms in the UK might relocate to other cities as large European and American banks adjust their locational strategies in Europe. Moreover, the competition for offshore RMB centres in Europe could be more intense. Many European cities, for instance Luxemburg, Frankfurt, Paris, have been trying to increase their roles as offshore RMB centres, even as London captures the current top spot as Europe's most important offshore RMB centre. Given the uncertainties surrounding Brexit negotiations, such competitive dynamics could change significantly as the Chinese government and Chinese state-owned banks turn their attention towards other European financial centres, in the interest of future stability.

With the continuing growth and internationalization of Chinese financial service firms, and increasing RMB internationalisation, the financial centres of Beijing, Shanghai and Shenzhen, which have the largest concentration of Chinese financial firms' headquarters (Lai, 2012; Pan et al., 2017), could become much more important within global financial centre networks. In fact, there is already stiff competition amongst these cities for leadership position within China's financial centre networks. While Brexit might not directly affect financial centres in mainland China, the more diversified locational choice of Chinese financial firms in Europe could improve the diversity and international connectivity of Chinese financial centres, since these cities can have direct connections through intra-firm linkages with more cities within Europe rather than with London.

Brexit's impact on Hong Kong would be more direct. As a leading financial centre in Asia, Hong Kong has long been a vital platform for foreign firms to invest in China as well as Chinese firms going abroad (Pan and Brooker, 2014). Moreover, Hong Kong's strong connections with London have also improved the attractiveness of London for Chinese firms entering European markets. Given Hong Kong's unique position in connecting the Chinese

economy with the London, uncertainties of the Brexit could negatively impact Hong Kong's gateway function, especially if more global financial giants leave London for other European cities. In fact, with the rapid development of financial centres in mainland China, the role of Hong Kong as a gateway financial centre is also threatened. Brexit could therefore accelerate the reconfiguration of banking and financial services activities in East Asia in ways that could favour mainland Chinese financial centres over Hong Kong.

As the other prominent financial centre in Asia, Singapore is likely to see less direct impact from Brexit in terms of the changing business activities of financial firms themselves. Instead, some impact might come from trade and foreign direct investments (FDI). Following the EU referendum, the depreciating Sterling and the strengthening Singapore Dollar has raised concerns over the competitiveness of Singaporean exports of manufactured goods and services, which might lead to lower demand for treasury, foreign exchange and insurance services out of Singapore. However, the impact has been limited as the UK ranks 22nd on the list of Singapore's key trading partners; the USA and other Asian countries are much more important in that respect. In comparison, the EU as a whole is Singapore's second largest trading partner. If Brexit negotiations and regulatory changes should drive economic and financial activities more towards European economies and financial centres, these could benefit Singapore's growth in financial activity in the longer term.

Brexit is also creating much uncertainty for start-ups, tech companies and innovative activities, pushing them away from the prolonged and messy negotiation of UK's EU exit towards other financial centres. New York will be a clear winner based on its current advantage in venture capital financing, but given the current rise of FinTech industries in Hong Kong, Singapore and especially the mainland Chinese market, we expect a significant shift in investment and industry interest towards Asian financial centres. FinTech does not only rely on financing capabilities and maturity of capital markets, it is also shaped by the depth and maturity of firms and actors in related industries, such as media, telecommunications and infrastructure, and regulatory environment, which supports innovative activities and intellectual property rights. These are well established in the financial centres of Singapore and Hong Kong, and have gained much traction in recent years in many Chinese cities. The booming internet economies in China and rapid emergence of new firms, payment systems, and financing platforms have created a very vibrant market for FinTech.

Elsewhere in this issue, Pollard calls for a reengagement of financial geography with political economic questions about the relationships between finance and economic

development. This concurs with our approach in organising the above discussion around trade, FDI, and strategies of non-financial firms in order to highlight the importance of wider economic linkages and production networks for studying the development of financial centres. Rather than just focusing on specific types of financial institutions (e.g. retail banks, investment banks, institutional investors), or specific financial markets (e.g. equity, commodity or derivatives markets), geographers need to pay greater attention to the ways in which other economic sectors and wider aspects of economic change can create important shifts in firm strategies and industry orientation. In the case of Brexit, impacts on trade and investments of non-financial firms will have significant impact on their demands the volume and types of financial services and the types of financial institutions and locations best suited to meeting those changing needs. Similarly, developments in other industries and changing financial ecologies could shape the emergence of new financial sectors such as FinTech and alternative financial platforms (Langley and Leyshon, 2017); this could reshape financial centre development not only in Asia but global financial networks.

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